STATE OF ILLINOIS

ILLINOIS COMMERCE COMMISSION

Illinois Commerce Commission	:	
On Its Own Motion	:	
	:	**17-0855**
Initiating Proposed Rulemaking Relating	:	
to the Regulatory Accounting Treatment	:	
of Cloud-Based Solutions.	:	

<u>DISSENT</u>

By Commissioners Bocanegra and Oliva, dissenting:

The Majority's decision in rejecting to enter a Second Notice Order and close this docket represents a missed opportunity at the Commission and for the ratepayers and citizens of Illinois to benefit from innovative technology that can improve the quality, efficiency and speed of utility services while cutting cost, reducing redundancies, and promoting the State's environmental goals. What began almost three years ago and then began yet again as an effort to explore innovative ways to encourage responsible and prudent investments into cloud-based computing solutions or computing service (hereafter, "Cloud Computing") has dwindled to nothing more than a circular and futile exercise in failed logic. The Majority's decision is in direct contradiction to a message issued to the public less than two weeks ago on June 26, 2020, wherein four of the five Commissioners, wrote *"Rest assured, grid modernization and innovation, among others, remain of tremendous importance to the Commission."* Less than a month later, the Majority's actions say otherwise.

Much like a cloud, the Majority's reasoning for denying the Proposed Rule is nothing more than fluff – an illogical, flawed and severely strained attempt at coming up with reasons to deny a Proposed Rule that achieved consensus among the parties to this docket, including consumer advocates. We dissent from the Majority's decision and address the wasted opportunity for Illinois consumers and the inconsistency in the Majority's professed reasons for denial.

A. Promoting Innovative Technologies and Solutions Is Essential to Improving the Quality and Efficiency of Utility Services while Reducing Costs

Regulators and utilities are responsible for ensuring reliable, safe, and affordable utility services. Utility regulation should not resist change but foster cutting-edge strategies and progressive energy policy. This has worked for Illinois in the past. Going as far back as the days of Samuel Insull, an American utility magnate known for creating Commonwealth Edison Co. in 1907 and contributing to the creation of an integrated electrical infrastructure in the United States, the electric grid in Illinois has seen considerable innovative developments, including the installation of advanced metering infrastructure, forward-thinking rate base structures such as performance-based ratemaking, decoupling, deregulated energy markets, and water system privatization laws. These technological and regulatory advancements have resulted in historically lower utility rates for Illinois consumers. Smart thermostat and energy efficiency incentives are additional recent examples of ways that utilities in Illinois, through regulation, have committed to helping consumers better manage their energy use, gain greater control over their monthly bills and help Illinois reach its clean energy and energy efficiency goals. Illinois has consistently worked to develop processes that allow new technologies to enhance and ensure grid modernization.

Today's decision sets Illinois back. The Illinois Commerce Commission's long history and global reputation for promoting innovation risks ending with the Majority's decision in this docket. It demonstrates that we are not a state that promotes and champions breaking new ground. Utilities provide a critical service and it is important that they make investments in modernizing their infrastructure in an equitable and cost-effective manner. The new Proposed Rule, Title 83, Chapter I, Subchapter b of the Illinois Administrative Code as Part 289, agreed to by Commission Staff and key stakeholders, would create the regulatory certainty needed for efficient long-term capital investments in Cloud Computing. Without the regulatory certainty of the Proposed Rule, there is less incentive for utilities to invest in Cloud Computing. The Majority's decision places Illinois on the sidelines, watching as other states foster Cloud Computing by utilities to enhance and improve utility delivery and services. These benefits include allowing for more efficient pooling and management of capacity, enabling customers to take advantage of the operational expertise of specialized technology companies, reducing the costs associated with new computing equipment and updating outdated software, and eliminating the risk of technological obsolescence, as cloud based software is easily and routinely updated.

B. The Proposed Rule Provides Numerous Benefits to Consumers and Utilities in line the Commission's Mission

Adoption of the modified Proposed Rule, which was drafted by Commission Staff and has consensus from the parties, including the Joint Utilities and Advanced Energy Economy Institute ("AEEI"), has many benefits, including promoting responsible and prudent utility investments into Cloud Computing, promoting reduction in other information technology expenditures, and furthering our State's ambitions relative to the energy and environment. Originally, this docket was initiated to determine whether creating a rule encouraging off-premise computing solutions via regulatory asset creation was acceptable compared to the status quo. While utilities can seek to have traditional on-premise solutions rate based as significant capital expenses, the same cannot be said for Cloud Computing, where such investments are typically paid on a subscription as a service ("SaaS") and treated as an operating expense. Migrating from on-premise to off-premise solutions and expecting utilities not to ask whether the same regulatory treatment can and should apply is precisely the regulatory lag we often seek to remedy. That utilities already may make investments in Cloud Computing misses the point of how such investments should be treated for regulatory purposes, especially to the extent it can promote and expand these services for the betterment of its customers.

Exploring this rulemaking provides not only consistency across all regulated utility sectors in terms of how this Commission looks at such investments by water, electric and gas utilities but also informs how we can expect our ratemaking processes to work. The Proposed Rule would provide regulatory certainty as to how those investments are treated for ratemaking purposes: as regulatory assets. The Proposed Rule, as with all utility expenditures, *does not guarantee* anything about how those financial investments in Cloud Computing are recovered. Utilities would still be required to show that such investments are prudent, reasonable, and least cost. Therefore, the Proposed Rule would encourage prudent off premise solutions while relaxing the regulatory treatment of those investments.

Encouraging investment in Cloud Computing further promotes Illinois' programs and investments in distributed generation, net metering, energy efficiency, Internet of Things, and smart grids, to name a few. In fact, our state already encourages investments into cloud computing for certain state agencies. *See* Open Operating Standards Act, 20 ILCS 45/15(g). Further, incenting these investments has beneficial environmental impacts, such as reducing a utility's carbon footprint and energy usage and encouraging dematerialization. By removing carbon emitting on-site computing solutions and migrating to cloud services, which is also increasingly powered by renewable resources, we further our State's carbon emission reduction goals. Cutting energy usage results in a reduction in load, KwH used, and capacity, all of which require less generation and reliance on carbon-emitting energy sources. Dematerialization, or replacing physical hardware with virtual hardware, further contributes to sustainability efforts and reduces future landfill waste.

Incenting Cloud Computing investments reduces rates both directly and indirectly. Directly, utilities can reduce operational side IT infrastructure costs, reducing expenses and allowing them to focus on their core function: providing reliable, affordable, and safe services. Indirectly, investments in Cloud Computing potentially further reduce rates by promoting economic efficiency of other programs, functions, and services, such as net metering, distributed generation, demand response, interconnection processes, curtailment services and electrification.

C. The Proposed Rule's "80/20 Split" is Not Arbitrary

When the rule was first submitted for notice and comment, it was returned by Joint Committee on Administrative Rules ("JCAR") for further evaluation. At its meeting on June 11, 2019, JCAR objected to the proposed rulemaking. In its Statement of Objection, JCAR explained that it was making the objection because it "ha[d] not yet received sufficient information regarding the economic impact of the rulemaking on affected ratepayers." On June 26, 2019, the Commission issued an order withdrawing the rulemaking to allow for time to address JCAR's objections.

On September 6, 2019, the Commission convened a public hearing. At this hearing, the Commissioners asked extensive questions to representatives for the utilities, energy policy groups, tech and software companies and Commission Staff to address how utilities break down and define what constitutes operating and maintenance ("O&M") expenses and what does not. Most if not all stakeholders suggested that such a task was simply not feasible.

Thereafter, ComEd filed a motion seeking an extension of the first notice period ("ComEd's Motion"). ComEd stated that additional time would allow the parties to convene further workshops at which the stakeholders could discuss the First Notice Rule. In ComEd's Motion, ComEd suggested that the extension of time would allow the parties "to come together, evaluate the proposed rule, build consensus, and when necessary, come up with alternatives." ComEd's Motion at 2. ComEd's Motion was granted without objection and Staff convened two additional workshops.

After conducting workshops, the resultant revised proposed language was as follows:

> *A public utility may record as a regulatory asset and, subject to the Commission's determination of prudence and reasonableness in a rate case, include in rate base eighty percent (80%) of the costs incurred from an outside service provider for a cloud-based computing solutions or computing service. if all the requirements in subsection (b) are met. The remaining twenty percent (20%) of such costs shall be recorded as an operating expense. All other costs associated with a cloud-based computing solutions or computing service, including but not limited to, implementation costs, training costs, and data conversion costs, shall be included in rate base or recorded as an operating expense in accordance with financial accounting requirements, Commission practice, rules, and law.*

While not privy to the stakeholder workshops, an educated guess suggests that the parties addressed the Commission's concerns that the original rule was overly broad because it failed to adequately break down capital expenses and operating expenses. The result was the 80/20 breakdown for recording cloud-based computing solutions as a regulatory asset in the Proposed Rule. This was not arbitrary nor pulled from the cloud (pun intended). To suggest that the parties to this docket, including Commission Staff, advocacy groups, and the Joint Utilities, simply came up with an arbitrary number is without merit, dismissive of their time, expertise and efforts, and denies our stakeholders the benefit of collective reasoning. As the Joint Utilities point out, the AG also recognized that a cost breakdown requirement would impose an undue burden on cloud software vendors that could in turn create problems for Illinois utilities and their customers. AG Post-Hearing Comments at 3 (Sept. 27, 2019). The filed comments suggest that the 80/20 was derived from fixed percentages used in other capitalization scenarios; namely, on-premise computing solutions.

Further, the Majority fails to explain why any other combination of numbers would suffice. For example, why would 79/21 have settled the matter? It can be no more 'arbitrary' than the 4% rule the California PUC imposed on such similar cloud investments or on the 25% rule advanced in England. In addition, the Majority suggests that the split is not based on a "sufficient set of data points" or "common industry practice" without necessarily stating or providing guidance on what amount of data is "sufficient" to their taste or illustrating how the Proposed Rule is at odds with "common industry practice." Further, the Majority claims both that the split provides little oversight for the Commission and impairs consumer advocates' ability to review costs. In arguing there is "little oversight," the Majority either glosses over or chooses to ignore the opening phrase of the 80/20 proposal: "*A public utility may record as a regulatory asset* ***and, subject to the Commission's determination of prudence and reasonableness in a rate case****, include in rate base…"*. (Emphasis Added). This is odd considering that the "prudence and reasonableness" analysis is at the core of every rates-related case before this Commission.

Additionally, the Majority claims to champion the concerns of consumer advocates. However, what could they be championing when we see no objection in this docket by any consumer advocate at any time to the Proposed Rule. Instead, it appears the Majority is substituting their views for those of consumer advocates, choosing to disregard the work and input of the stakeholder workshops that included consumer advocates, who as discussed above do not appear to oppose the Proposed Rule. Finally, and perhaps the biggest irony here is that when this was returned by JCAR, the Commission asked the parties to be specific in breaking down expenses and yet, now that the parties have fashioned a breakdown of capital and operating expenses, the Majority complains it goes too far.

D. Section 289.40(a) Does Not Guarantee Rate Base

Any claim that the proposed language in 289.40(a) guarantees rate base without further inquiry is simply baseless and contravenes the most basic of common sense and traditional pillars of ratemaking principles. Adopting the Proposed Rule is not guaranteeing rate base – the Proposed Rule is merely written to provide regulatory certainty of how such investments are accounted for in ratemaking. Any indicia by the Majority that the Proposed Rule somehow guarantees recovery without further inquiry glosses over the fact that 289.40(a) provides that a utility "*may* record such investments as a regulatory asset," "*subject to* the Commission's determination of prudence and reasonableness." (emphasis Added).

Further, 289.40(b)(1) provides that "The public utility shall record as a regulatory asset *only costs incurred* through the period being reported, including prepayments…" In other words, reading the Proposed Rule as a whole, such investments, if recorded as a regulatory asset, can be rate based up to 80% subject to prudency and reasonableness review and subject to only that which was actually paid and prepaid. (emphasis Added).

Thus, any potential concern regarding expensing pre-paid services are misplaced given that such types of expenses are incurred and reviewed in the normal course of ratemaking. Take, for example, annual insurance premiums, often paid up front and in full. To the extent a prepaid Cloud Computing solution is terminated early, it would stand to reason that the Commission would conclude that such cancelled, refunded or unpaid services would no longer be *used and useful* assets and thus removed from rate base. The Dissent is unable to imagine a situation where 1) a utility would actually suggest that such cancelled prepaid services remain in rate base; 2) a party would fail to argue that such cancelled prepaid services are no longer used and useful; and 3) the Commission would fail to examine such a fact. The fact that the Proposed Rule fails to explicitly state the obvious – that cancelled prepaid services are likely subject to a finding that such investments are no longer used and useful – neither condones the possibility of such a scenario nor circumvents fundamental principles of rate making.

E. Conclusion

In conclusion, the ALJ correctly found that staff and stakeholders have come to a consensus on language for Part 289 and that the Commission should approve the Second Notice Order and Appendix for a new Part 289, which comports with the consensus reached in this proceeding. That consensus and collaboration of stakeholders highlights the positive public reception of the Proposed Rule and the thoughtfulness that went into redrafting in a manner consistent with the concerns raised by the Commission and JCAR. The concerns expressed by JCAR were and are appropriately addressed in the comments filed in this docket, none of which were addressed today by the Majority. The time and effort by Staff, the Joint Utilities and concerned stakeholders has been disregarded by the Majority and this is truly a tragedy for Illinois consumers and the grid they rely on for essential utility services.

The Majority argues that the timing of the rulemaking is not appropriate because of the current COVID-19 pandemic and a new docket on "uncollectibles." In its own ironic reasoning, the Majority provides no evidence how the Proposed Rule affects, addresses or intersects with the other issues or dockets. At best, the Majority argues it is unclear how the Proposed Rule could affect rates and, therefore, we should avoid addressing the issue. This reasoning is flawed for two very important reasons. First, the Commission has direct control over how the Proposed Rule will affect rates through its review and deliberation in rate and reconciliation cases. Second, improvement to the grids that bring clear benefits to consumer, the performance and efficacy of utility services, and environmental benefits should not be disregarded because there is some uncertainty around their fiscal impact, especially when the Commission can determine the impact. Arguing that this is "bad timing" is simply misleading and sets a dangerous precedent for allowing vague externalities such as "the current crisis," to not only influence judicial decisions but to also impede regulation itself.

However, pressing and known concerns, such as achieving Illinois's clean energy goals, will require utilities to process huge data sets from renewables, storage, and energy efficiency programs and for managing distributed energy resources. Cloud-based computing solutions facilitate the foreseeable demand management and grid monitoring required to manage a smart grid. All of this is more effectively and rapidly accomplished through cost recovery incentives for investments in Cloud Computing.

We conclude our Dissent by offering the following observation: innovation is not just the technologies and processes that allows utilities to deliver the most effective, safe, efficient, reliable, and least cost services, but also the regulatory framework regulatory commissions provide that allows innovation to occur. What we see in the Majority's decision is the failure of our Commission to keep our part of the compact to ensure a regulatory space that promotes and incents progress. We are truly disappointed to see such a missed opportunity for Illinois consumers here, especially when our colleagues so recently declared how this Commission values innovation. Perhaps in words, but not in practice.

For the foregoing reasons, we respectfully dissent.